

VIRTUAL BOARD MEETING MINUTES: August 22, 2023 ABC Headquarters

Call Meeting to Order at 10:07* a.m.

Attendees

Board Chair Tim Hugo
Board Vice-Chair Robert Sledd
Board Member Greg Holland *
Board Member William Euille
Board Member Mark Rubin *
Chief Executive Officer, Travis Hill
Chief Government Affairs Officer, John Daniel
Chief of Law Enforcement, Tom Kirby
Chief Retail Operations Officer, Mark Dunham
Chief Digital and Brand Officer, Vida Williams
Chief Administrative Officer, David Alfano
Chief Transformation Officer, Elizabeth Chu
Chief Information Officer, Paul Williams

Deputy Secretary to the Board, Chris Curtis
Director of Finance, Doug Robinson
Office of the Attorney General, Jim Flaherty
Executive Assistant, Kathleen LaMotte
Eric Moeller, Chief Transformation Officer, Commonwealth of Virginia
Tony Lee, Deputy Transformation Officer, Commonwealth of Virginia

* Mr. Holland and Mr. Rubin were present in person

Introductory Remarks

Chair Hugo thanked all for attending the virtual meeting and further thanked CEO Hill and CTO Alfano for their work since the July meeting. Charman Hugo felt there was a lot that the Commonwealth Chief Transformation Office (CTO) and ABC were in agreement upon and appreciates the collaboration and the work of the Authority staff, and the work of the Administration.

Mr. Hill introduced the 2024 Amended Operating Budget. The Board approved a budget at the last meeting, but there was a request to look for efficiencies and the ability to grow profitability. The Authority worked internally and with the Governor's CTO office. This amendment preserves the investment in Authority employees around bonuses, training, and professional development. Additional savings include vacancies that have been open for more than a year, and work with retail team to find efficiencies in store man-hours. The Authority continues to invest in its law enforcement regulatory capabilities, making sure we honor that commitment to our stakeholders. This budget proposal seeks to fill 45 positions, 32 of which are sworn officers. The Authority will continue to build back the enforcement capabilities that are necessary to regulate the market. The Authority also seeks to continue to invest in inventory and order management and expand e-commerce capabilities.

Approve FY2024 Amended Budget

CAO Alfano reported that:

- Reviewed the Profit and Loss statements of what was previously approved vs. the amended budget put forth today.
- This budget reflects net profit of \$244.3 million. He reviewed the specific changes from the original budget that included restored employee training and bonuses and increased efficiencies in retail along with a reduction in vacant positions. Mr. Alfano is confident the Authority can continue to operate under these efficiencies.
- Recruiting has been challenging for Enforcement, but with recent investments, the Authority will be better able to fill vacant positions. With the Authority focusing on fewer projects, there is a need for less contract labor employees.

Mr. Holland asked if the budget would still allow for the Authority to hire outside counsel if needed. Mr. Daniel replied that most years it is not needed. Last year 's spend was only about \$20,000 and this should not be impacted by this budget.

- The Authority worked with the Commonwealth CTO, Mr. Moeller, and Deputy CTO, Tony Lee, to review opportunities for greater efficiencies to yield greater profitability. Mr. Sledd requested updates going forward on how the efforts are going and what the findings are.

Mr. Rubin asked if the Board will potentially be re-visiting the budget throughout the year and reconsider what is being done on a regular basis? Mr. Alfano advised that the Authority is seeking endorsement of this budget, but throughout the year as the analysis is completed on these activities and identify if there are additional opportunities to take action and continue to compare actual to budgeted performance and call out any differences as a result of these actions.

Mr. Rubin stated that the budget process needs to come to an end. The Authority's sole focus should not be maximizing profit. No organization can function well when they are continuously revising the budget. This is not a necessary revision due to lack of funds.

Mr. Hugo agreed and that the discussions originally began because there was agreement at the last meeting between the Authority and the CTO. The budget can't be amended each month, but if there are other ideas through the year, those will be ideas for next year's budget.

- Mr. Alfano reviewed potential budget risks. Management will continue to monitor and take action if needed.

Mr. Holland requested to hear the GACRE presentation prior to voting on the budget which may address his concerns surrounding operating cost reductions.

Approve Governor's Advisory Council on Revenue Estimates (GACRE) Forecast

Travis Hill introduced the presentation. This forecast for the next five years has the ABC profits trending as an increase of net profit as a percentage of net revenue as discussed as a target in the last Board meeting. Expenses are being kept flat to down, there are a few savings strategies combined with revenue growth. In out years, investments in HR systems and setting aside funds for an incentive program are planned.

Dave Alfano reported that:

- The starting point for GACRE was the 2024 budget with some assumptions for out years. The main driver is projected revenue growth of 5%. This year there was revenue growth attributable to 2% volume increase, 1.5% price increase, and 1.5% on premiumization. The Authority used those same estimates to determine

potential future revenue growth. Operating expenses are expected to be at or below current levels based on efficiencies available, returning the Authority back to the profitability levels of previous years.

- Assumptions for GACRE forecast also included a 1% growth in miscellaneous revenue and licensing fee growth, consistent with prior years.

Mr. Rubin expressed concerns that 5% may be too optimistic. With the planned cuts to marketing (which influences premiumization) and store staffing cuts which may negatively impact the customer experience, there is the likelihood that 5% growth is not attainable. The Authority's ability to withstand online ordering and changes in habits in how younger generations relate to alcohol must be considered. Past growth could be attributed to pandemic spikes and may not be tenable in the future. Mr. Hill advised that ahead of the COVID pandemic, growth was 6 – 7% annually and spirits are commanding more of a market share over beer and wine. Mr. Alfano added that the GACRE forecast may be updated in future years.

Mr. Robinson addressed a concern about cost inflation by advising that about 1.5 - 2% is a price increase at the wholesale level finding its way into the top-line based on how the Authority's markup formula is implemented.

Mr. Hugo brought up a pre-COVID initiative for retail employees to grow sales, which was suspended during the pandemic and there is an opportunity for retail employees to help grow sales. Mr. Hill advised that it is an opportunity, and we are re-emphasizing it with employees and it may also help reduce store shrink by engaging with customers.

- Based on meetings with the Governor's economic advisors, a "soft landing" from recession perspective, and the assumption of 2% for inflation was used as a moderate estimate. Some categories such as freight and rent are higher, and they are large operational expense categories.
- Healthcare assumptions are provided by the State, and they are updated every two years.
- New store growth is estimated at four new stores annually.
- The salary and wage assumptions of 1% are based on some feedback around previous salary actions taken at ABC. Budget language will be brought forth to allow the Authority to deviate from the budget for across the board state raises and to allow the Authority to implement pay for performance. This will provide flexibility to do more or less than other state raises. \$800,000 was added in addition to existing funding for an employee incentive program to give the Authority more flexibility to recognize higher performers.

Mr. Rubin hopes the issue of 1% pay raises will be revisited. The Board did vote for pay for performance in light of the circumstances known at the time, but it may need to be re-examined to establish a more coherent plan. Incentives and pay for performance is a good thing and we need to make it work of our employees in light of the tight labor market.

Mr. Sledd said compared with other state employees, ABC was way above state increases in recent years.

Mr. Rubin responded that prior to the 2021 actions, the ABC Authority was not competitive with the marketplace and we must maintain the competitive nature.

- The vacancy factor is customized for each division rather than applying a flat percentage across the Authority. Most divisions range between 2 – 3%, IT has a higher vacancy factor of 5%, and Enforcement is 9%.
- As positions become vacant this year and future years, a decision will be made if the positions must be backfilled or if the Authority may operate without them.

Board member Euille moved to approve the FY2024 Amended Budget, and Vice-Chair Sledd seconded.

Mr. Rubin commented that he is reluctantly voting for the budget, as it is needed for the Authority to move forward. The Authority staff has done a good job meeting the objectives but still doesn't feel it is a great budget. This has been a dysfunctional process to come up with a budget. There were several mis-steps since April, but the process could be

improved greatly and re-set if we were to reestablish how ABC is supposed to function. Mr. Rubin read from § 4.1-101, “...there is hereby created an independent political subdivision of the Commonwealth, exclusive of the legislative, executive, or judicial branches of state government, to be known as the Virginia Alcoholic Beverage Control Authority... The Board of Directors of the Authority is vested with control of the possession, sale, transportation, distribution, and delivery of alcoholic beverages in the Commonwealth, with plenary power to prescribe and enforce regulations and conditions under which alcoholic beverages are possessed, sold, transported.... The exercise of the powers granted by this subtitle shall be in all respects for the benefit of the citizens of the Commonwealth and for the promotion of their safety, health, welfare, and convenience...” It is not stated in the code that our job is to maximize profits. We do our absolute best at it as it is part of our responsibility, but not our only responsibility. Just as stakeholders stated in a letter to the Chair, they see the priority as Enforcement, but there needs to be a re-set of the relationship between the administration and the ABC, and his hope is that it will be recognized during the next budget process.

Mr. Hugo responded that he looks forward to working with everyone on the Board to look for a mutually acceptable reset that will be for the good of the citizens of the Commonwealth.

Mr. Holland seconded what Mr. Rubin stated, and also said that we are also not only stewards of the Commonwealth of Virginia, but also to our stakeholders and employees. The first amended budget was woefully inadequate on that front and the vote in July did not fall short of their duty to the citizens of Virginia as has been suggested. He hopes that next year we will take a different approach on this.

The motion passed on a roll-call vote of 5 – 0.

Mr. Euille moved to approve the GACRE submission, and Mr. Sledd seconded the motion. The motion passed on a roll-call vote of 5 - 0

Public Comment

None

Comments from the Board

Meeting Adjournment

Meeting adjournment at 11:14 a.m.

